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April 17, 1997

William F. Caton
Federal Communications Commission
1919 M Street, N.W., Room 222
Washington, D.C. 20554

Re: Expedited Reconsideration of Commission's Interpretation of Section 272(e)(4)
CC Docket No. 96-149

Dear Mr. Caton:

Enclosed for filing in this docket are the original and three copies of the Bell Company Comments on Expedited Reconsideration of Interpretation of Section 272(e)(4). Please date-stamp and return the extra copy in the enclosed envelope.

We are also sending a copy of these comments to Janice Myles of the Common Carrier Bureau and to ITS, Inc., as directed in the Commission's Public Notice of April 3, 1997.

If you have any questions concerning this matter, please contact me at (202) 326-7902.

Sincerely,

Michael Kellogg

Michael K. Kellogg

Enclosures

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION

Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, As Amended	CC Docket No. 96-149

BELL COMPANY COMMENTS ON EXPEDITED RECONSIDERATION OF INTERPRETATION OF SECTION 272(e)(4)

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April 17, 1997

EXECUTIVE SUMMARY

1. The Commission must adhere to the unequivocal text of section 272(e)(4), which expressly provides that a Bell operating company "may provide any interLATA or intraLATA facilities or services to its interLATA affiliate" (47 U.S.C. § 272(e)(4)), so long as it meets the statutory nondiscrimination and cost allocation requirements. Adhering to the plain language of section 272(e)(4) creates no conflict with the separate affiliate requirement of section 272(a). Section 272(a) establishes a general rule, and the subsections that follow detail the conduct that Congress understood to be consistent with that general rule. Subsection (e)(4) makes clear that a BOC may provide interLATA services and facilities to its affiliate without breaching the rule of section 272(a).

In addition, the language of section 272(a) itself separately makes clear that Congress did not intend to prohibit such conduct. A separate affiliate is required only for activities that qualify as "[o]rigination of interLATA telecommunications services." When a BOC provides interLATA services to its affiliate under subsection (e)(4), it does not "originate" interLATA services; rather, the affiliate "originates" such services when its retail customers place interLATA calls. Thus, under section 272(a), if a BOC wishes to "originate" interLATA services for consumers, it must do so "through" its affiliate. One way in which it may do so is to provide the underlying interLATA services and facilities "to" its affiliate in accordance with section section 272(a).

2. As Dr. William Taylor explains in his attached affidavit, moreover, giving effect to the plain language of section 272(e)(4) will have strongly pro-competitive effects.

First, barring BOCs from providing services and facilities to their affiliates would harm customers by depriving them of the "lower costs and higher quality services that flow from an integrated supplier." Taylor Aff. ¶ 4 (Tab 1).

Second, preventing BOCs from achieving these cost savings would not provide any countervailing benefits to customers in other markets. "Whatever the merits of [competitive] concerns with respect to exchange access, . . . there is no possibility that a BOC could use its supply of wholesale interLATA services to its affiliates to impede competition in the retail interLATA market." Taylor Aff. ¶ 8. That is because no BOC currently supplies interLATA service in-region and "no BOC possesses market power in the supply of those services." Id.

Third, abundant historical evidence shows that competition has succeeded in telecommunications markets that are equally or more susceptible to anti-competitive tactics than the interLATA market. Id. ¶ 12. History also demonstrates that safeguards like those contained in section 272 are successful. Id. ¶¶ 11, 19. In fact, the Commission itself has recognized that such protections are "'an effective alternative to structural separation for protection against anticompetitive conduct.'" Id.¶ 19 (quoting Computer III Remand, 6 FCC Rcd 7571, 7576 (1991)).

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION

Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, As Amended	CC Docket No. 96-149

BELL COMPANY[1] COMMENTS ON EXPEDITED RECONSIDERATION OF INTERPRETATION OF SECTION 272(e)(4)

When Bell Atlantic and Pacific Telesis asked the D.C. Circuit to reverse summarily the Commission's interpretation of section 272(e)(4) in its First Report and Order,[2] the Commission declined to defend its ruling. Instead, it requested, and received, a remand in order to give full consideration to the plain language arguments presented to the court of appeals by Bell Atlantic and Pacific Telesis.

Now that its request has been granted, the Commission's task is a simple one: It must adhere to the unequivocal text of section 272(e)(4) and must therefore conclude that a Bell operating company "may provide any interLATA or intraLATA facilities or services to its interLATA affiliate" (47 U.S.C. § 272(e)(4)), so long as it meets the statutory nondiscrimination and cost allocation requirements. That is what the statute says, and the Commission has no choice but to honor the unambiguous congressional directive.

[1] These Comments are submitted on behalf of the Bell Atlantic Telephone Companies, Bell Atlantic Communications, Inc., BellSouth Corporation, NYNEX Corporation, SBC Communications Inc., Southwestern Bell Telephone Company, Nevada Bell, and Pacific Bell.

[2] First Report and Order and Notice of Proposed Rulemaking, Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, As Amended, CC Docket No. 96-149, FCC 96-489 (Dec. 24, 1996) (hereinafter "First Report and Order").

Accordingly, while we welcome the opportunity to address the policy questions raised by the Common Carrier Bureau — and to demonstrate that the proper interpretation of section 272(e)(4) is, in fact, strongly pro-competitive — such questions are ultimately beside the point. Congress, in the plainest possible language, authorized BOCs to provide any services and facilities to their interLATA affiliates. The Commission cannot revoke that authority even if, for policy reasons, it would prefer a different result.

I. CONGRESS UNAMBIGUOUSLY EMPOWERED BELL OPERATING COMPANIES TO PROVIDE INTERLATA SERVICES AND FACILITIES TO THEIR INTERLATA AFFILIATES

1. Section 272 of the Communications Act specifies the manner in which Bell operating companies may provide interLATA services once they receive section 271 approval to do so. In particular, section 272(a) provides that, to take full advantage of its section 271 authority, a BOC must create a separate interLATA affiliate and must act "through" such an affiliate (47 U.S.C. § 272(a)(1)) in providing certain specified services to consumers. Id. § 272(a)(2)(B) (enumerating those services).

The remainder of section 272 describes the permissible relationship between a BOC and its interLATA affiliate. Among other things, the section contains a series of "structural and transactional requirements" designed to ensure the affiliate's independence and to make all transactions between the companies transparent, so that any problems of discrimination or cost misallocation can be readily identified. See id. § 272(b) (requiring, among other things, that the affiliates maintain separate books and accounts, have separate officers and directors, and conduct all transactions with the BOC "on an arm's length basis with any such transactions reduced to writing and available for public inspection").

The provision at issue here, section 272(e)(4), identifies one specific aspect of the permissible relationship between a BOC and its interLATA affiliate. The text of subsection (e)(4) speaks for itself. It says that a Bell operating company "may provide any interLATA or intraLATA facilities or services to its interLATA affiliate if such services or facilities are made available to all carriers at the same rates and on the same terms and conditions, and so long as the costs are appropriately allocated."

That language provides a conclusive answer to the question on remand. The Bell companies seek only what the statute explicitly grants them: the right to "provide any interLATA or intraLATA facilities or services to [their] interLATA affiliate[s]." The provision is written in "ordinary English," and the Commission has no proper alternative but to apply the statute according to its unambiguous terms. Barnett Bank of Marion County, N.A. v. Nelson, 116 S. Ct. 1103, 1111 (1996). See also MCI Telecommunications Corp. v. AT&T Corp., 114 S. Ct. 2223, 2233 (1994) (Commission has no power to "alter the meaning of the Federal Communications Act of 1934").

The language of subsection (e)(4) is no less plain — and no less binding on the Commission — merely because Congress also made abundantly clear in the same provision that a BOC may provide intraLATA, as well as interLATA, facilities and services to its affiliate. There is nothing unusual about Congress providing an added dose of clarity to remove any conceivable doubt on a question. That is especially true here, where the legislature was creating a new relationship, making it especially important to specify precisely what conduct is, and is not, permissible in order to avoid any potential confusion or litigation. Indeed, it would be bizarre to conclude that, because Congress went out of its way in section 272(e)(4) to make absolutely clear that BOCs have extremely broad authority to provide "any" services and facilities to their affiliates (as well as other companies), the provision should be read to grant no authority at all. See Public Notice ¶ 2 (suggesting this as a possible result).

2. Because the natural understanding of section 272(e)(4) so evidently favors our conclusion, no serious attempt has been made to base a contrary argument on the actual language of section 272(e)(4) itself. As the Commission has acknowledged, the First Report and Order did not adequately consider the provision's plain language. And, when the issue reached the court of appeals, our opponents — AT&T and other IXCs who benefit enormously from stifling long-distance competition from Bell companies — sought only to avoid the clear terms of the provision. Those parties argued that section 272(e)(4) must be read to mean something other than what it plainly says in order to avoid a supposed conflict with other provisions, chiefly section 272(a). See, e.g., AT&T Response to Motion for Summary Reversal or Expedition at 7 ("AT&T Opp.").

The conflict is wholly imaginary. Section 272(a) establishes a general rule providing that BOCs may provide certain services only "through" an interLATA affiliate. The subsections that follow detail the conduct that Congress understood to be consistent with that general rule. And section 272(e)(4) specifies, in the most direct terms, that it is consistent with Congress's understanding of the separate affiliate requirement for an operating company to provide interLATA services or facilities to its own affiliate, so long as it also provides the same services to others on nondiscriminatory terms. Far from conflicting with section 272(a), section 272(e)(4) makes clear that a BOC may provide interLATA services and facilities to its affiliate without breaching the rule of section 272(a). This, standing alone, is a complete answer to the supposed conflict imagined by the IXCs.

In addition, the language of section 272(a) itself separately makes clear that Congress did not intend to prohibit such conduct. Section 272(a) provides that a separate affiliate is required only for activities that qualify as "[o]rigination of interLATA telecommunications services." When a BOC provides interLATA services to its affiliate under subsection (e)(4), however, it is not "originating" interLATA services. Rather, it is the affiliate that "originates" such services when its retail customers place interLATA calls.

Thus, under section 272(a), if a BOC wishes to "originate" interLATA services for consumers, it must do so "through" its affiliate. But the BOC may provide the underlying interLATA services and facilities "to" its affiliate, as long as it does so on a nondiscriminatory basis. Indeed, one of the most natural ways that a BOC would originate interLATA services for consumers "through" an affiliate is by providing the underlying interLATA services and facilities "to" that affiliate. Nothing in the language of section 272(a) requires the affiliate to act as a self-provider of the interLATA services that it originates for consumers. And section 272(e)(4) in fact makes clear that the affiliate may look to the BOC for the underlying interLATA services and facilities that it needs for the "[o]rigination of interLATA telecommunications services."[3]

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[3] This understanding of "origination" in section 271(a) is entirely compatible with the statement in section 271(b)(1) that a BOC or its affiliates "may provide interLATA services originating in any of its in-region States." In section 271(b), the term "originating" is used simply to identify the geographic location where "interLATA services" begin. See § 271(b)(2) (providing a different rule for "services originating outside [a BOC's] in-region States"). In section 272(a), by contrast, "origination" refers to the specific activity of providing interLATA services to the customers who initiate interLATA calls.

Even if there were some doubt on this score — that is, even if the Commission were to perceive a conflict between section 272(a) and section 272(e)(4) that is not apparent on the face of those provisions — the result would be no different. Under well-established canons of statutory interpretation, the specific authorization contained in section 272(e)(4) would take precedence over the general language of section 272(a).[4] "However inclusive may be the general language of a statute, it will not be held to apply to a matter specifically dealt with in another part of the same enactment. . . . Specific terms prevail over the general in the same or another statute which otherwise might be controlling." Fourco Glass Co. v. Transmirra Products Corp., 353 U.S. 222, 228-29 (1957) (internal quotation omitted). See also Morales v. Trans World Airlines, Inc., 504 U.S. 374, 384 (1992) ("it is a commonplace of statutory construction that the specific governs the general").

This deeply rooted rule of construction has particular resonance here, where the proffered alternative interpretation of section 272 runs roughshod over the language of section 272(e)(4), the more specific statutory provision. As the Commission will recall, its initial decision in this matter concluded that section 272(e)(4) was actually a limitation on BOC authority. On that understanding — which the IXCs, but not the Commission, continued to champion in the court of appeals — section 272(e)(4) restricts the manner in which BOCs may provide the small subset of interLATA services that other statutory sections permit them to provide directly even without section 271 approval and prevents a BOC from leasing its facilities to its own affiliate and other

[4] As the titles of the two subsections themselves make clear, subsection 272(a)(1) merely establishes a "general" requirement, while the provisions of subsection 272(e) dictate how the BOC should/may fulfill "certain" specific requests.

carriers. See First Report and Order ¶¶ 261, 266 & n.669. But, as demonstrated in the court of appeals, this interpretation ignores every salient feature of section 272(e)(4).

First, and most basically, this reading disregards the fact that nothing in section 272(e)(4) suggests that it is intended to constrain BOC authority. On the contrary, unlike all the other parts of section 272(e) — which uniformly provide that the operating company and/or the affiliate "shall" or "shall not" take specific actions — subsection (e)(4) states that a BOC "may provide" interLATA services and facilities to its affiliate (and to other carriers as well). That is quite evidently a crucial difference in statutory terminology, and one that cannot be squared with the statutory reading urged by the IXCs.

Second, the alternative reading ignores the equally important fact that — far from mentioning a few discrete interLATA services — section 272(e)(4) explicitly grants authority to provide "any" such services. The plain meaning of the term "any" undermines any attempt to cabin section 272(e)(4)'s relevance to a handful of discrete services that are never even referred to in that provision.[5]

Third, nothing in section 272(e)(4) remotely suggests that public auctions must be held if a BOC wants to allow its affiliate to use existing facilities. The statute allows BOCs to "provide" such facilities to its affiliate. That term makes clear that the company may retain ownership of such facilities and "ma[ke] available" those facilities to all carriers on a

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[5] See Fleck v. KDI Sylvan Pools, Inc., 981 F.2d 107, 115 (3d Cir. 1992) ("The word 'any' is generally used in the sense of 'all' or 'every' and its meaning is most comprehensive.") (internal quotation omitted), cert. denied, 507 U.S. 1005 (1993). See also Shea v. Vialpando, 416 U.S. 251, 260 (1974); Harrison v. PPG Indus. 446 U.S. 578, 589 (1980).

nondiscriminatory basis. Indeed, section 272(e)(4)'s cost-allocation requirement would have no point if BOCs could engage only in one-time transfers of title.

In sum, even if the Commission were to conclude that there is some ambiguity about the meaning of section 272(a), the Commission has no license to resolve that ambiguity in a way that turns the plain language of section 272(e)(4) on its head. That provision is specific and precise, and any conceivable conflict here must be resolved by giving effect to its evident meaning. See Fourco Glass, supra.

3. In their attempt to avoid the plain meaning of section 272(e)(4), the IXCs also offered a variety of other arguments in the court of appeals. None has merit.

MCI asserted in the D.C. Circuit that the natural understanding of section 272(e)(4) could not be accepted because it would render superfluous section 272(g)(2), which provides that a BOC may market or sell the interLATA services provided by its affiliate. See MCI Opposition to Motion for Summary Reversal or Expedition at 7-8. MCI apparently believes that allowing a BOC to provide interLATA services to its affiliate would automatically allow it also to market such services on behalf of its affiliate. That, of course, is not true. In any case, marketing is not itself an "interLATA service" within the scope of subsection (e)(4).[6] Accordingly, subsection (g)(2) provides operating companies with authority different from, and not subsumed within, that provided by subsection (e)(4).

There is similarly no basis for AT&T's suggestion that adherence to the plain language of subsection (e)(4) would undermine section 271(a)'s requirement that Bell operating companies

[6] See 47 U.S.C. § 153(21) (defining "interLATA service" as "telecommunications between a point located in a [LATA] and a point located outside [that LATA]"); 47 U.S.C. § 153(43) (defining "telecommunications" as "the transmission . . . of information").

obtain FCC authorization before providing long-distance services. AT&T Opp. 10. As explained in the court of appeals, section 271(a) makes clear that "[n]either a Bell operating company, nor any affiliate of a Bell operating company, may provide interLATA services except as provided in this section" (emphasis added). Since section 272(e)(4) obviously is not "in [that] section," it cannot be read as an exception to section 271's authorization requirement.[7]

Finally, the IXCs err in their more general contention that our straightforward reading of section 272(e)(4) renders meaningless the interim separation requirements in section 272. To the contrary, the separation requirements continue to provide a significant additional layer of protection against any theoretical concerns about possible anticompetitive conduct. As noted above, section 272 is designed to make entirely transparent the dealings between an operating company and its interLATA affiliate. Its comprehensive separations requirements — including its requirement that all transactions between the two be conducted on an arm's length basis, be publicly disclosed, and be subjected to a biennial Federal/State audit, 47 U.S.C. § 272(d) — make it easy to identify any possible violations of the statute's nondiscrimination rules. See 47 U.S.C. § 272(c).

Moreover, by requiring BOCs to offer services and facilities to competitors on the same terms they offer them to their affiliates, section 272 provides an effective additional deterrent against cross-subsidization. BOCs will have no conceivable incentive to subsidize their affiliates where the price of doing so is subsidizing all the affiliates' competitors as well. And

[7] To clarify a point that was disputed in the court of appeals, when this matter was last before the Commission, Pacific Telesis did, in fact, make clear that BOCs would have to receive section 271 approval before providing interLATA facilities and services to their affiliates. See Pacific Telesis Ex Parte Comments (Nov. 27, 1996).

this is supplemented, of course, by the requirement in section 272(e)(4) that the BOC appropriately allocate its costs. In short, none of the protections created by section 272 is in any way compromised by adherence to the plain meaning of section 272(e)(4).

II. ADHERENCE TO THE EVIDENT MEANING OF SUBSECTION (e)(4) WILL GREATLY ENHANCE LONG-DISTANCE COMPETITION

As we explained at the outset, the issue for the Commission in this case is not one of policy. Congress has already made the relevant policy choice by specifying, in extraordinarily clear language, that Bell operating companies may provide facilities and services to their affiliates so long as the operating companies do not discriminate and properly allocate the relevant costs. The Commission has no authority to alter that rule even if it would have preferred a different result. And, in particular, it lacks authority to mandate a different result on the theory that, despite section 272(e)(4)'s explicit prohibition, BOCs will, in fact, discriminate and misallocate costs. The Bell companies have no choice but to adhere to those express statutory requirements (and, of course, fully intend to do so). Speculation that the companies will violate their legal obligations provides no conceivable basis to ignore the plain meaning of section 272(e)(4).

In any case, as Dr. William Taylor explains in his attached affidavit, adherence to the text of section 272(e)(4) will actually have strongly pro-competitive effects.

First, barring BOCs from providing services and facilities to their affiliates would harm customers by depriving them of the "lower costs and higher quality services that flow from an integrated supplier." Taylor Aff. ¶ 4 (Tab 1). See also Declaration of James G. Cullen ¶ 6 (Tab 2) (stating that requiring duplicate facilities would raise Bell Atlantic's long distance costs by "50 to 70 percent"); Declaration of Phillip J. Quigley ¶ 5 (Tab 3) ("the cost to Pacific Telesis of purchasing all of its long distance capacity from a major facilities-based provider is at least 40 percent higher than the cost of using our own facilities to transmit long distance calls"). Indeed, as Professor Taylor has stressed, IXCs are currently taking advantage of the economies of scope created by just such integration as they enter local telephone markets. Taylor Aff. ¶ 6. For "consumers [to] benefit from competition," BOCs must also be able "to us[e] [their] own services — including interLATA services — when scope economies make them the efficient choice." Id.

Second, preventing BOCs from achieving these very substantial cost savings would not provide any countervailing benefits to customers in other markets. The only conceivable basis that has been proffered for preventing BOC participation in the interLATA market is their market power in exchange access markets. Id. ¶ 7. But that justification provides no basis for preventing BOCs from providing interLATA services and facilities to their affiliates: "Whatever the merits of those concerns with respect to exchange access, . . . there is no possibility that a BOC could use its supply of wholesale interLATA services to its affiliates to impede competition in the retail interLATA market." Taylor Aff. ¶ 8. That is because no BOC currently supplies interLATA service in-region and "no BOC possesses market power in the supply of those services." Id.

Indeed, since there is no dispute that BOCs now may also provide exchange access to their affiliates, there is no conceivable basis for preventing the BOCs from providing interLATA services to those affiliates. "Any supposed risk to competition when the BOC provides wholesale interLATA services to its affiliate -- for which the BOC has no current market share or market power -- is certainly less than when the BOC provides exchange access -- arguably a bottleneck service in some markets -- to its long distance affiliate." Id. ¶ 9. Thus, if it "makes sense to permit the latter, it must make sense to permit the former." Id.

Third, a decade of history supports the conclusion that there is no policy basis for preventing BOCs from providing interLATA services and facilities to affiliates. There is abundant historical evidence that competition has succeeded in a host of telecommunications markets that are equally or more susceptible to anti-competitive tactics than the interLATA market. Id. ¶ 12. In particular, competition has thrived after BOC participation in the cellular, voice messaging, corridor and intraLATA long-distance, and customer premises equipment markets, among others. Id. ¶¶ 12-18.

History similarly demonstrates that safeguards like those contained in section 272 are successful. Id. ¶¶ 19-20. In fact, the Commission itself has recognized that such protections are "'an effective alternative to structural separation for protection against anticompetitive conduct.'" Id.¶ 19 (quoting Computer III Remand, 6 FCC Rcd 7571, 7576 (1991)).

Fourth, the Commission has asked whether the risk of discrimination differs depending on whether a BOC provides bundled "end-to-end" or more discrete services to its affiliate. As Professor Taylor explains, neither situation presents a problem that is not already addressed by the comprehensive safeguards provided by the Act. Id. ¶¶ 21-22. Because the exchange access component of any "bundled" interLATA service, as well as the end-to-end interLATA service itself, must be made available to competitors on nondiscriminatory terms, there simply is no way that the BOC could use the pricing structure of a bundled service to provide its affiliate with a competitive advantage. Id. As a result, there is no policy justification for prohibiting BOCs from providing interLATA services to their affiliates, regardless of the form in which those services are provided.[8]

[8] The Commission has requested that BOCs clarify how they will use any available capacity in their official services network. The BOCs' use of such capacity will depend upon market conditions and capacity constraints faced by each BOC at the time of section 271 approval. Accordingly, it is not possible to state with precision at this time how such capacity will be used. For illustrative examples, however, see the attached Declaration of Hardy F. Moebius (Tab 4).

Respectfully submitted,

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April 17, 1997

BEFORE THE

FEDERAL COMMUNICATIONS COMMISSION

WASHINGTON, D.C. 20554

In the Matter of	)	
	)	
Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended;	)	**CC Docket No. 96-149**
	)	
and	)	
	)	
Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area	)	

AFFIDAVIT OF WILLIAM E. TAYLOR

1. I am Senior Vice President of National Economic Research Associates, Inc. (NERA), head of its telecommunications economics practice and head of its Cambridge office. My business address is One Main Street, Cambridge, Massachusetts 02142.

2. I have been an economist for over twenty-five years. I received a B.A. degree in economics (Magna Cum Laude) from Harvard College in 1968, a master's degree in statistics from the University of California at Berkeley in 1970, and a Ph.D. in Economics from Berkeley in 1974, specializing in industrial organization and econometrics. I have taught and published research in the areas of microeconomics, theoretical and applied econometrics, and telecommunications policy at academic institutions (including the economics departments of Cornell University, the Catholic University of Louvain in Belgium, and the Massachusetts Institute of Technology) and at research organizations in the telecommunications industry (including Bell Laboratories and Bell

Communications Research, Inc.). I have participated in telecommunications regulatory and judicial proceedings before state public service commissions, the Federal Communications Commission (FCC), the Canadian Radio-Television and Telecommunications Commission and state and federal courts concerning competition, incentive regulation, price cap regulation, productivity, access charges, pricing for economic efficiency, and cost allocation methods for joint supply of video, voice and data services on broadband networks. I filed affidavits regarding economic aspects of the implementation of Section 272 of the Act in CC Docket No. 96-149 on August 18 and November 14, 1996 where copies of my vita are supplied.

I. SUMMARY AND CONCLUSIONS

3. On remand in this proceeding, the FCC has issued a notice that asks a series of questions relating to Section 272(e)(4) of the Telecommunications Act which states simply that

> [a] Bell operating company and an affiliate that is subject to the requirements of section 251(c)...may provide any interLATA or intraLATA facilities or services to its interLATA affiliate if such services or facilities are made available to all carriers at the same rates and on the same terms and conditions, and so long as the costs are appropriately allocated.

The purpose of this affidavit is to address the issues raised by the FCC's Notice from an economic standpoint. I conclude that there is no economic reason to restrict the supply of interLATA services by a BOC to its interLATA affiliate beyond the nondiscrimination requirements of the Act and in fact such restriction would be harmful.

4. Specifically, I find that:

- Additional restrictions would harm customers. Long distance customers benefit from the lower costs and higher quality services that flow from an integrated supplier, and the BOCs' competitors—as they vertically integrate into local exchange markets from long distance—face no such restrictions on the ability of one part of their enterprises to serve another.

- Additional restrictions would serve no useful purpose and would not protect competition in any market. The BOC's supply of interLATA services that are freely available from multiple suppliers to its affiliate poses no threat to the competitive process. Indeed, there is less concern with the BOC's supply of interLATA services than with the supply of exchange access is expressly permitted under the Act. From an economic perspective, there is no relevant distinction between exchange access and other interLATA services such as transport, operator services or billing and collection, with the possible exception that in some geographic areas there may be fewer alternative sources of supply for exchange access. If supplying exchange access to its affiliate is not anticompetitive, then supplying other, more competitively available interLATA services to its affiliate cannot be anticompetitive.

- Competition has thrived in actual markets in which BOCs supply services to their downstream affiliates or divisions. Long experience in real markets has shown that vigorous competition can be sustained under such conditions. In addition, the Commission's nonstructural safeguards have been tested and found to be sufficient to detect and prevent cross- subsidization.

- The nature of the wholesale interLATA service in question—whether offered in isolation or as part of an end to end service -- has no bearing on the ability of the BOC to discriminate or to cross-subsidize. As long as competitors can obtain services they need that only the BOC can provide on the same terms and conditions that the BOC affiliate obtains them, there can be no threat to the competitive process. Because the exchange access component of any discrete or combined interLATA service can always be separately identified and supplied under identical terms and conditions to all competitors, the BOC has no additional ability to discriminate or cross-subsidize when discrete or combined interLATA services are supplied to its affiliate.

II. BARRING BOCS FROM PROVIDING INTERLATA SERVICES AND FACILITIES TO THEIR LONG DISTANCE AFFILIATES WOULD HARM CONSUMERS.

5. To economists, rules that restrict transactions between firms or between organizations within a firm are costly to consumers, in that they necessarily raise the cost of supplying the final goods or services. Nonstructural separations requirements are a pragmatic attempt to accommodate and reconcile the increased efficiency of integrated supply with the procompetitive need to ensure that some transactions occur at arm's length. While there may be disagreement among the parties on the competitive consequences of these arrangements, there is little disagreement that there are significant cost savings that can be attained by supplying multiple services on an integrated basis. Thus, permitting BOCs to supply in-region interLATA services to their affiliates can decrease unit costs by allowing the BOC to expand the use of its facilities and services by additional customers, achieving economies of scope.

6. Economies of scope—cost savings from supplying multiple services with the same personnel and facilities—are an important competitive advantage in telecommunications markets which can reduce the cost of providing services. As long distance carriers integrate into local exchange markets, they can supply their local and long distance offerings in whatever way is most efficient, using the lowest-cost combination of their own facilities in the most efficient way possible, whether in combination with the BOC's network facilities and services or not. In fact, AT&T already has announced that it is using its existing 4ESS long distance switches to provide combined local and long distance in the form of its Digital Link Service. In order that consumers benefit from competition, the BOC, too, must be able to piece its services together using commercially available services when they are cost-effective and using its own services—including interLATA services—when scope economies make them the efficient choice.

III. BARRING BOCS FROM PROVIDING INTERLATA SERVICES AND FACILITIES TO THEIR LONG DISTANCE AFFILIATE WOULD NOT PROTECT COMPETITION IN ANY MARKET.

7. The Telecommunications Act of 1996 already incorporates a number of provisions that are designed to protect against any theoretical risk that a BOC might be able to use whatever market power it has over the provision of exchange access to impede competition in the interLATA market. For example, a BOC (i) can originate interLATA telecommunications services in-region only after the Commission has found that it has met a checklist which opens the local market to entry by competing providers of local exchange and access service; (ii) can provide such services only through a separate affiliate; and (iii) in doing so must comply with a number of non-discrimination and cost allocation requirements set out in the Act.

8. These various provisions of the Act address concerns raised during the debate over the Act that the BOCs could use their status as a supposed bottleneck provider of exchange access to limit long distance competition. Whatever the merits of those concerns with respect to exchange access, which I have addressed elsewhere, there is no possibility that a BOC could use its supply of wholesale interLATA services to its affiliate to impede competition in the retail interLATA market. First, no BOC today supplies interLATA service in-region, and no BOC possesses market power in the supply of those services. Thus there is no market power in the upstream

market (in this case, wholesale interLATA services) that the BOC could attempt to leverage into the retail interLATA market.

9. Second, each BOC is expected to supply exchange access to its interLATA affiliate and is required to supply it to its affiliate's long distance competitors. If it is not anticompetitive for a BOC to supply its affiliate with exchange access service, it cannot be anticompetitive for it to similarly provide other interLATA services to its affiliate—services for which the BOC has no market power and for which there can be no concern that a bottleneck monopoly will be leveraged into the retail interLATA market. Any supposed risk to competition when the BOC provides wholesale interLATA services to its affiliate—services for which the BOC has no current market share or market power—is certainly less than when the BOC provides exchange access—arguably a bottleneck service in some markets—to its long distance affiliate. When it makes sense to permit the latter, it must make sense to permit the former.

10. To be clear, Section 272(e)(4) does not merely affirm, in economic terms, that a BOC's supply of wholesale interLATA service to its affiliate is not anticompetitive whenever its supply of exchange access to that affiliate is not anticompetitive. Rather, in conjunction with the other parts of Section 272(e), subsection (4) mandates that wholesale interLATA facilities or services be supplied in a nondiscriminatory manner subject to the rules in Section 272(b-d) and subject to the Commission's cost allocation procedures. Wholesale interLATA services here are explicitly treated the same as facilities and services supplied by the BOC to its affiliate, as outlined in subsection 272(e)(2). While the fact that the services in question are not bottleneck services means that there is no realistic risk of anticompetitive behavior if the BOC supplies them to its affiliate, the nonstructural safeguards provide still another layer of protection to ensure that the interLATA affiliate does not receive a subsidy.

IV. ACTUAL MARKET EXPERIENCE SHOWS THAT ALLOWING BOCS TO PROVIDE INTERLATA SERVICES AND FACILITIES TO THEIR LONG DISTANCE AFFILIATE PRESENTS NO RISK OF HARM TO COMPETITION

11. Over a decade of experience has shown (i) that competition thrives when a BOC supplies both exchange access and a retail service for which competitors require exchange access and (ii) that